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The Manufacturers Hanover
Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

MONDAY, AUGUST 31, 1981 VOLUME XVIII, NUMBER 35

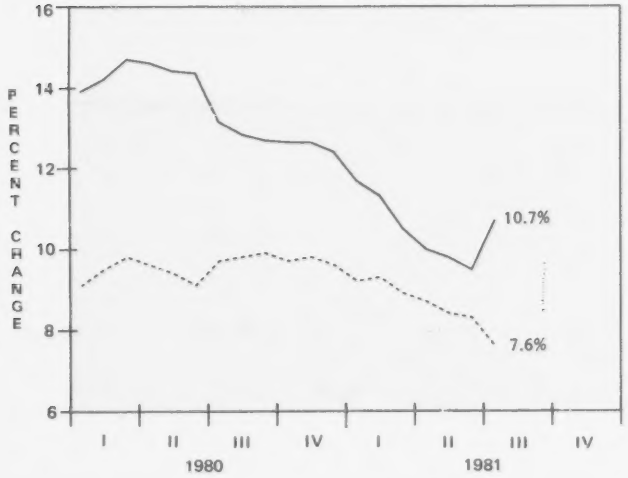
The Rebound In The Rate Of Inflation . . .

Although the July rise in the consumer price index represents the largest monthly increase in 16 months, it does not necessarily indicate that the moderating trend in the rate of inflation has come to a halt. In July, the CPI rose by 1.2 per cent, month-over-month, up from the 0.7 per cent increase posted in June. An examination of one of the fastest rising components of the CPI—housing—along with the way the index is put together, suggests that the rate of consumer price inflation in July may not have been as bad as it initially looked.

For one thing, the CPI appears to overstate the cost of housing which includes not only the cost of furnishing and maintaining a home, but also its financing—primarily house prices and mortgage interest rates. But since most people do not buy a home every month, or even every year, including increases in both mortgage interest rates and home purchase prices in the CPI causes it to overstate the effects of inflation on day-to-day household budgets.

CHART I

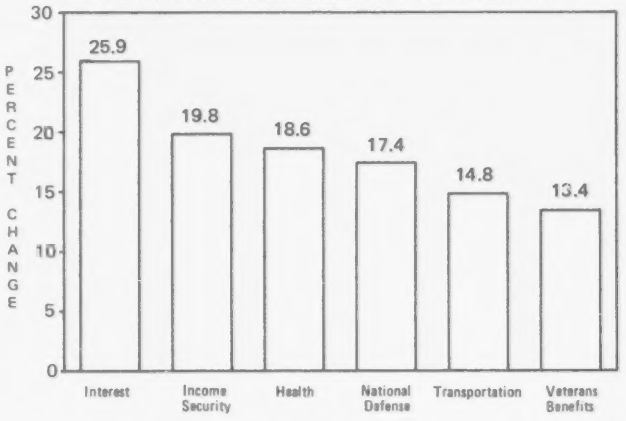
12-MONTH PERCENT CHANGE IN CPI (LINE) VS. 12-MONTH PERCENT CHANGE IN CPI EXCLUDING HOME PRICES AND FINANCING (DOT)



What is more, the CPI has not taken into account the steep slump in home sales in recent months. Since so few people have been buying homes recently, the relative share, or "weight," of the home financing component in the index (which is based on 1972-1973 spending patterns) is now probably much too high compared with earlier years, and thus influences the overall CPI more than it should.

CHART II

PERCENT CHANGE IN THE SIX LARGEST COMPONENTS OF THE FEDERAL BUDGET: FISCAL 1981 TO DATE VS. COMPARABLE FISCAL 1980 PERIOD



Financing costs rose 3.2 per cent in July, resulting from a 1.8 per cent rise in house prices and a 1.3 per cent increase in mortgage interest rates. When the influence of these components is eliminated, the rise in the CPI slows significantly—from a 1.2 per cent rate of rise, month-over-month, to only 0.7 per cent. When year-to-year comparisons are made, the divergence is also striking (see Chart I). Whereas the original index spikes sharply upward, back to a double-digit rate of inflation, the 12-month increase in the CPI excluding home prices and financing has shown a steady improvement since the beginning of the year.

Food prices rose 0.8 per cent in July, following a 0.2 per cent increase in June and a decline in the preceding month. Although some acceleration in the rate of rise in food prices was expected to occur due to reduced supplies of red meats (Financial Digest—July 6, 1981), this component received an unexpected boost from higher prices of fruits and vegetables—primarily a result of the medfly infesta-

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tion in California. Prices of fruits and vegetables jumped 2.3 per cent during the month, following declines in May and June. Importantly, meat prices increased by two per cent in July, due to sharply curtailed supplies of beef and pork.

. . . May Not Be So Bleak After All . . .

Recently, ranchers have been sending fewer cows to market than earlier this year, preferring instead to increase placements in feedlots and breeding herds. However, the upward pressures on beef prices should ease in the fourth quarter. Many of the animals which were put into feedlots at the beginning of this year will have reached maturity and will be slaughtered—thus increasing supplies at meat counters.

Similarly, hog producers have been curtailing pork production. This has been done to avoid a repeat of operating losses experienced by farmers during most of last year when production reached record levels, prices sank and operating costs skyrocketed. In July, pork prices jumped almost five per cent compared with June, and they currently stand almost 16 per cent above year-ago levels.

A significant determinant of meat supplies, and consequently their prices, is the cost and availability of feed grains. Feed grain prices affect meat prices through their influence on livestock profitability. The Department of Agriculture now expects feed grain production—corn, sorghum, oats and barley—to exceed last year's crop by 19 per cent. Due to

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 8/19/81	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	134.378	+ 2.717	+ 4.851
Loans to Depository Inst.	1.457	+ .186	+ 1.112
Float	2.681	– 1.020	– 3.380
Total Reserve Bank Credit	148.147	+ 1.879	+ 7.219
Treasury Deposits with Federal Reserve Banks	2.974	– .640	– .656
Currency Outside Banks	125.428	+ .832	+ 6.803
Member Bank Reserves:			
Required	41.298	+ 1.416	+ .710
Excess (Deficiency)	.217	– .105	– .107
Total Reserves Held	41.515	+ 1.311	+ .603
Net Borrowed Reserves	1.009	+ .283	+ .994
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	91.752	+ .245	+ 9.242

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M-1B	430.8	– 0.9‡	+ 6.7‡
M-2 (July '81)	1,760.9	+ 5.2	+ 9.1
M-3 (July '81)	2,090.3	+ 8.9	+ 11.6
L (May '81)	2,476.0	+ 7.2	+ 11.0

†Seasonally adjusted. *Seasonally adjusted annual rate. ‡Four-week moving average.

New York Money Market

Offering Rates 8/28/81	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	15.55%	15.58%	14.90%
* Federal Agencies	16.10	17.00	16.05
* Project Notes—Taxfree (46% Taxable Equivalent)	14.91	16.67	NA
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	17.70	17.95	18.40

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	15.25%	Sep.	17.25%
15- 29 days	16.00	Oct.	17.10
30- 59 days	17.25	Nov.	16.80
60- 89 days	16.75	Dec.	16.75
90-179 days	15.75	Jan.	16.65
180-239 days	15.75	Feb.	16.55
240-270 days	14.00		

‡Industrial Paper—Prime		†Federal Funds	
30- 89 days	17.00%	Effective Rate	16.10%
90-120 days	17.00		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'81	$ 2,882	$ 2,853	$ 2,565
Gross National Product (1972 Dollars)*	2nd Q'81	$ 1,507	$ 1,516	$ 1,463
Percent Change, Annual Rate	2nd Q'81	– 2.4%	8.6%	– 9.9%
Change in Consumer Prices (all urban consumers)*	Jul '81n	14.4%	8.4%	1.2%
Change in Producer Prices*	Jul '81	4.8%	7.2%	20.4%
Civilian Employment (Thousands of Persons)†	Jul '81	98,962	98,392	96,999
Unemployment as % of Civilian Labor Force†	Jul '81	7.0%	7.3%	7.6%
Personal Income*	Jul '81	$ 2,422	$ 2,385	$2,161
Leading Indicators Composite Index (1967=100)†	Jul '81n	133.7	133.9	128.1
Industrial Production Index (1967=100) †	Jul '81	153.4	152.9	140.4
Net Change in Consumer Installment Credit†	Jun '81	$ 1.93	$ 1.35	–$ 2.04
U.S. Merchandise Trade Balance †	Jun '81	–$ 2.10	–$ 2.44	–$ 1.91
Plant and Equipment Expenditures*	3rd Q'81	$322.88(a)	$317.29(a)	$296.23
Private Housing Starts (Thousands of Units)*	Jul '81	1,055	1,021	1,277
New Construction Expenditures*	Jun '81	$ 236.2	$ 239.7	$ 218.5
Total Business Inventories†	Jun '81	$ 493.5	$ 490.3	$ 464.2
Total Business Sales†	Jun '81	$ 353.0	$ 349.2	$ 305.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. a-Anticipated.

improved weather conditions, corn production alone could be 16 per cent greater than last year's drought-affected crop. In addition, the food grain harvest--wheat, rye and rice--is forecast to be 16 per cent higher than last year, with wheat production expected to reach a record high of 2.75 billion bushels.

The expectation of a favorable harvest of food and feed grains this year has already depressed prices of many crops. At the end of August, corn prices were 17 per cent below their end-March quotes and sorghum prices fell 33 per cent during the same period. Traditionally, lower grain prices have resulted in a greater number of animals being put into feedlots, ultimately expanding supplies at the meat counter.

Finally, the index for transportation increased 0.8 per cent in July, following increases averaging less than 0.2 per cent in the preceding three months. Substantial increases in the index for public transportation and used cars were primarily responsible for this jump. Intracity mass transit fares rose 14.7 per cent during the month, reflecting sharp increases in public transit fares in a number of metropolitan areas, including New York, Chicago and Los Angeles. When combined with large increases in airline, intercity bus and taxi fares, this resulted in a 6.3 per cent increase in the public transportation component during July, compared with June.

. . . But Budget Prospects Remain Dismal

The upturn in the rate of consumer price inflation

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (8/12/81)	128,656	+ 1,193	+36,639
New York City (8/12/81)	30,679	– 106	+ 9,495
Commercial Paper (8/12/81)	156,094	+ 1,843	+33,337

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (8/12/81)	183,558	– 674	+23,465
New York City (8/12/81)	53,714	– 572	+ 6,301

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (8/12/81)	446,883	– 1,896	+47,172
New York City (8/12/81)	106,897	– 1,279	+16,641

Financial Markets

	Friday 8/28/81	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	16.00%	– .20	+ 6.05
180-Day Bills†	16.80	– .05	+ 6.54
Longest Bills†	16.75	+ .19	+ 6.56
Recent Issues:			
16¼s 8/31/83	16.58	+ .38	
14s 6/30/85	16.00	+ .25	
14⅞s 8/15/91	15.21	+ .31	
13⅞s 5/15/11	14.41	– .24	
Municipals:			
Bond Buyer–20 Bond Index* (8/27/81)	12.97%	+ 1.03	+ 4.12
Blue List Total ($ Million)	$ 729	– $ 71	+ $ 88
30-Day Visible Supply ($ Million)	$1,718	– $265	– $1,253
Total	$2,447	– $336	– $1,165
Corporates:			
Moody's Aa Composite (8/27/81)	15.68%	+ .31	+ 3.20
30-Day Visible Supply ($ Million)	$7,937	+ $345	+ $4,403
Stocks:			
Dow-Jones Averages:			
Industrials	892.22	– 28.35	– 40.37
Transportation	375.46	– 20.33	+ 55.35
Utilities	109.74	– 2.99	– 1.22
65 Stocks	350.22	– 13.34	+ 9.46
Standard and Poor's 500 Stocks	124.08	– 5.15	– 14.81
N.Y.S.E. Composite Index	71.97	– 3.13	+ 1.44
N.Y.S.E. Avg. Daily Vol. for Week (000's)	44,724	+ 3,960	+ 5,726

* 46% Taxable equivalent 24.02%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 8/28/81	Week Ago
Overnight	17.25%	10.88%
1 month	18.25	11.44
3 month	18.50	12.50
6 month	18.75	12.69
1 year	18.00	12.69
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	15.20%	12.05%
Long Term (7 to 15 yrs.)	15.10	12.35

FOREIGN EXCHANGE SPOT RATES

New York Opening (8/28/81)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02476	40.38
Canada	.8294	1.2057
Denmark	.1292	7.7378
France	.1690	5.9155
Germany	.4055	2.4663
Italy	.0008130	1230.00
Japan	.004336	230.65
Mexico	.04018	24.89
Netherlands	.3650	2.7395
Switzerland	.4658	2.1470
U.K.	1.8372	.5443

was not the only discouraging economic news released last week. According to the Treasury Department, red ink again dominated the Federal budget in July. During the month, expenditures exceeded revenues by $10.3 billion which, although $4.7 billion less than the July, 1980 deficit, still brought the fiscal year-to-date red ink total to $59.7 billion. As a result, if the Reagan Administration's official estimate of a $55.6 billion deficit for the entire fiscal year is to be met, Washington will have to take in more than it spends in August and September. On the other hand, a continuation of the trends of the first ten months would produce a budget deficit for the fiscal year as a whole of $60 billion—or about ten per cent higher than the Administration's current estimate.

Unfortunately, prospects for a significant improvement in the Federal budget outlook are not bright. Despite the added emphasis being placed on national defense, the largest proportion of the fiscal year-to-date spending increase—more than 40 per cent of the $73 billion year-over-year gain—is accounted for by stepped-up income security outlays, such as inflation-indexed Social Security payments. The rise in national defense spending, in contrast, accounted for about 27 per cent of the overall spending increase.

But while the rise in income security outlays and defense spending has been widely publicized, the even faster growth in interest payments on the ever-expanding Federal debt has not (see Chart II on the first page). Interest payments are currently averaging more than $1.4 billion per month higher than year-earlier levels, and could reach $81 billion for the fiscal year as a whole. This total would be more than 25 per cent greater than interest outlays in fiscal 1980—and equivalent to approximately $360 for every man, woman and child in the United States.

Thus, in the absence of additional nondefense spending cuts in fiscal 1982, it appears likely that higher levels of defense spending and interest outlays, together with sizable personal and business tax cuts, will only widen the Federal deficit further. This, in turn, implies little relief for the financial markets any time soon. H

THE CORPORATE TRUSTEE ENDURANCE TEST.

DURABILITY:
When picking a corporate trustee for a bond issue—whether you're a corporation or municipality—pick carefully. Because you're going to have to live with that trustee a long time.

Manufacturers Hanover is one of the nation's largest and most experienced bond trustees. We have the expertise to anticipate problems before you even close the issue. By identifying trouble spots early, everything will run more smoothly. Year after year.

SUREFOOTEDNESS:
As corporate trustee, Manufacturers Hanover moves quickly in handling the day-to-day administrative tasks of overseeing a bond issue.

We consistently meet the NYSE and SEC requirements for the prompt transfer of certificates from seller to buyer. With TRANSIFAC,™ our electronic nerve center, each entry of data is "key verified"—entered twice by two different operators and then compared automatically by computer. It's the most accurate bondholder record-keeping system available.

ADAPTABILITY:
If a new or unusual change suddenly affects your company, Manufacturers Hanover reacts quickly in interpreting and analyzing indenture provisions. We know the alternate ways of handling many situations to help ensure the continued workability of the issue.

SENSE OF DIRECTION:
Our operations center is located in the heart of Wall Street, where most security trades take place—a location that facilitates the issuance and transfer of certificates for both you and your bondholders.

DETERMINATION:
No corporate trustee is more committed to service than Manufacturers Hanover. In addition to your own individual account officer, a backup officer—familiar with the requirements of your account—is ready to help you. Anytime.

If you want a corporate trustee who can meet every test, talk to Manufacturers Hanover. For more information on our whole range of indenture trusteeship services, call Joseph Unger, Vice President, at (212) 623-7542. Or write us at 40 Wall Street, New York, N.Y. 10015.

IF YOUR TRUSTEE CAN'T PASS IT, TALK TO MANUFACTURERS HANOVER.